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C O N F I D E N T I A L SECTION 01 OF 02 KUWAIT 001762

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DEPT FOR EB; PASS TO USTR JBUNTIN

E.O. 12958: DECL: 12/26/2017
TAGS: EFIN EINV ETRD ECON
SUBJECT: TAX ON FOREIGN COMPANIES REDUCED FROM 55 TO 15
PERCENT

REF: A. KUWAIT 107

¶B. KUWAIT 1573
¶C. KUWAIT 1590
¶D. KUWAIT 1741
¶E. KUWAIT 1760

Classified By: CDA Alan Misenheimer for reasons 1.4 (b) and (d)

¶1. (C) Summary: On December 26, Kuwait's National Assembly passed a bill to reduce the tax rate on foreign companies from 55 percent to 15 percent to attract more foreign investment. In making its case for passage of the law, the government noted that Kuwait attracted less than USD 300 million in foreign investment last year compared to USD 18 billion for Saudi Arabia. The new 15 percent tax rate will be applied as a flat tax on the annual net profits of foreign companies, unlike the previous system which incorporated a series of tranches that progressively reached a maximum of 55 percent. Capital gains on stock market investments will be exempt as will the profits of Kuwaiti distributors of foreign goods. This is a significant positive development for American companies in Kuwait and deserves favorable recognition during the President's January 2008 visit. End Summary

¶2. (U) On December 26, Kuwait's National Assembly passed a long-stalled and much-anticipated bill to reduce the tax rate on foreign companies from 55 percent to 15 percent. The law is expected to take effect in January, once it is approved by the Amir. The 36-17 vote amended Law Number Three of 1955, which was passed when Kuwait was still a British protectorate. Law Number Three was enacted to impose a 55 percent tax on the earnings of foreign oil companies at a time when oil companies were virtually the only foreign companies operating in Kuwait. Financial and Economic Affairs Committee Chairman Ahmed Baqer told reporters that the new 15 percent tax rate, designed to attract more foreign investment, would be applied as a flat tax on the annual net profits of foreign companies, unlike the previous system which incorporated a series of tranches that progressively reached a maximum of 55 percent. Background on tax holidays for foreign investors, restrictions on foreign ownership, and problems with Kuwait's previous tax code can be found in Post's 2007 Investment Climate Statement (Ref. A).

Application of new tax law

¶3. (U) Post has not yet translated the new law, but according to government press releases and local reporting, the new legislation applies a 15 percent tax rate to profits from:

- contracts executed fully or partially in Kuwait;
- selling leasing, or exploiting any trademark, patent or copyright;
- commissions;
- industrial or commercial business;
- selling real assets;
- selling real estate;
- rents; and
- services.

Income is to be computed after deducting expenses for salaries, fees, donations, depreciation, and amortization. Losses from a previous year can be deducted from current profits for tax purposes.

¶4. (U) Approval of the law came after strong opposition from a number of MPs who apparently did not object to the reduction in rate but felt that it should also apply to Kuwaiti distributors of foreign goods, who remain exempt. The government argued that taxing distributors would result in higher prices for consumers. The law will, however, be applied to Kuwaiti agents of foreign firms who act as the sole representative of their foreign partners. The new law will also apply to foreign franchises dealing with Kuwaiti agents, but, importantly, not to the capital gains of foreign entities trading either directly or indirectly in stocks listed on the Kuwait Stock Exchange. (Note: Previous ambiguity as to whether foreign entities would have to pay a 55% tax on capital gains has served as a major disincentive to inward foreign portfolio investment. The clarification provided by the new law brings Kuwait into conformity with the other GCC countries, none of which applies a capital gains tax, although Saudi Arabia applies a 5 percent withholding tax.)

Important step to attract FDI; More reforms needed
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¶5. (U) Finance Minister Mustafa Al-Shamali told the Assembly that Kuwait attracted less than USD 300 million in foreign investment last year compared to USD 18 billion for Saudi Arabia. (Note: The latest UNCTAD report puts Kuwaiti inward FDI at only USD 110 million, the lowest in the GCC.) Al-Shamali also said the law aims to attract foreign technology and expertise. Baqer added that the new tax law is part of a series of economic bills that will be passed by the National Assembly in a bid to transform Kuwait into a regional hub for trade and finance.

Comment

¶6. (C) At a time when friction between the government and National Assembly has largely resulted in a legislative deadlock (Refs B-E), the passage of this long-awaited tax reform is a welcome development. As we have highlighted to the GOK through TIFA talks and frequent discussions on economic reform, problems with the Kuwaiti tax regime have been a major irritant to American companies operating in Kuwait and a major deterrent to American companies considering investment in Kuwait. The government's decision to finally push through this legislation merits favorable U.S. recognition, including during the POTUS visit scheduled for January 2008.

¶7. (C) Looking ahead, the USG must sustain the push for other key economic legislation on privatization, public-private partnerships, disposition of state properties, labor reform, protection of intellectual property rights, and liberalization of Kuwait's hydrocarbon sector. While passage of this tax reform measure does not signal a surge of economic reform legislation in the offing -- indeed, the domestic political circumstances still appear discouraging -- it does give the Amir a significant positive factor to

consider as he ponders whether to dissolve the
under-performing National Assembly and call for new
elections.

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